

## **VERMONT STATE TEACHERS' RETIREMENT SYSTEM**

Meeting of the Board of Trustees

May 21, 2003

### **Board members present:**

JOSEPH MACKEY, Chairperson (Active No. 29334), term expiring July 1, 2005  
JAY KAPLAN, Association of Retired Teachers of Vermont, term expiring July 1, 2004  
JON HARRIS, Vice-Chairperson (Active No. 25669), term expiring July 1, 2003  
THOMAS CANDON, representing Commissioner of BISHCA, John P. Crowley  
VAUGHN ALTEMUS, representing Interim Commissioner of Education, David Larsen  
JEB SPAULDING, Vermont State Treasurer

### **Also attending:**

Dick Charleton, Ellen Griggs, Doug Moseley, Michael Lee and David Watts, New England Pension Consultants (NEPC)  
Marie Duquette, Director of Investment Services  
David Minot, prospective Director of Investment Services  
June Atwood and Rita Rinehardt, Vermont Retired Teachers' Association  
Cynthia Webster, Director of Retirement Services

Mr. Mackey called the meeting to order at 8:15 a.m. on Wednesday, May 21, 2003, in the Treasurer's Office Conference Room #1, Montpelier, Vermont.

### **ITEM 1:** Approval of minutes

**On a motion by Mr. Kaplan seconded by Mr. Harris, it was unanimously voted to approve the February 19, 2003, minutes as amended.**

**On a motion by Mr. Kaplan seconded by Mr. Candon, it was unanimously voted to approve the February 20, 2003, minutes as amended.**

The format of the minutes was discussed. It was the consensus of the board to allow minority opinions of motions to be qualified by a simple explanation if desired by the board member(s). Otherwise the minutes should be complete and concise.

**On motion of Mr. Kaplan seconded by Mr. Altemus, it was unanimously voted to approve the March 19, 2003, minutes as amended.**

**On motion of Mr. Candon seconded by Mr. Harris, it was unanimously voted to approve the April 9, 2003, minutes.**

Mr. Spaulding introduced Mr. Minot, the newly hired Director of Investment Services. Mr. Minot will be joining the Treasurer's Office on June 2, 2003. Mr. Kaplan introduced Ms. Atwood and Ms. Rinehardt, representing the Vermont Retired Teachers' Association.

### **ITEM 2:** Policy Guidelines – New England Pension Consultants

Ms. Griggs reviewed the policy guidelines, explaining the contents of each section, and going over in detail the various points of discussion. It was the consensus of the board to delete the mandate that the Board members provide details of all contact with managers, consultants, custodians and any other vendors as outlined under the *Ethics Report* on page 28.

**On a motion by Mr. Candon seconded by Mr. Altemus, it was unanimously voted to approve the revised Policy Guidelines.**

**On motion of Mr. Spaulding seconded by Mr. Kaplan, it was unanimously voted to amend the eighth bullet in the *Investment Manager* section of the Policy Guidelines to replace the word “Ensuring” with “Seeking”.**

**On motion of Mr. Altemus seconded by Mr. Candon, it was unanimously voted to approve all changes and exceptions in the Policy Guidelines as recommended by the managers with the exception of moving to high yield at this time.**

**ITEM 3:**      Liability Study – New England Pension Consultants

Michael Lee provided an overview of the revisions to the original liability driven asset allocation study presented in November of 2002, based on the results of the five year experience study. NEPC recommended Mix B as follows:

<b>Equity:</b>		<b>55%</b>
Large Cap	-	27%
Small Cap	-	12%
International	-	13%
Emerging	-	3%
<b>Fixed Income:</b>		<b>33%</b>
Domestic Bonds	-	21%
High Yield Bonds	-	5%
Global Bonds	-	7%
<b>Real Estate</b>		<b>6%</b>
<b>Hedged Strategies</b>		<b>3%</b>
<b>Alternatives</b>		<b>3%</b>

The expected return of Mix B was 8.5% and the expected risk was 10.7%. Mr. Kaplan questioned whether the additional liability as a result of the five year experience study will be reflected in the unfunded liability or the normal cost of the system. Mr. Lee stated he expected it would affect both.

The board discussed the action plan outlined by NEPC for transition to the recommended asset allocation mix. **Mr. Spaulding moved and Mr. Harris seconded a motion to accept Mix B as an asset allocation target but not to move into new asset classes without specific board approval. Mr. Kaplan vote nay; the remaining board members voted aye. Motion carried.** Mr. Kaplan stated he voted nay because as a fiduciary, he finds it difficult to accept

an asset allocation mix that includes hedge funds before the board has discussed them and fully understands them. Other board members indicated they understand they are not committed to moving into hedge funds, but by approving Mix B are providing an opportunity to become more knowledgeable on the asset class.

**On motion of Mr. Spaulding seconded by Mr. Harris, it was unanimously voted to allow Loomis to invest up to 10% of their total portfolio in below investment grade securities.**

**On motion of Mr. Kaplan seconded by Mr. Altemus, it was unanimously voted to increase Delaware's global bond portfolio from 5% to 7%.**

**On motion of Mr. Kaplan seconded by Mr. Harris, it was unanimously voted to allow Delaware to hold up to 15% of their portfolio in emerging markets on an opportunistic basis.**

**Mr. Spaulding moved and Mr. Candon seconded a motion to increase the allocation to small cap equity from 5% to 12%, split between growth and value, with the money to be taken from the large cap equity allocation. Mr. Kaplan voted nay; all others voted aye. Motion carried.**

**ITEM 4:** Quarterly Review – New England Pension Consultants

Dick Charleton provided an overview of the investment environment. All of the benchmarks reflect positive returns. The dollar is declining, but global bonds and emerging markets are up. High yield bonds lead the pack.

The total fund return for the quarter ending March 31, 2003, was (1.3%). Over the last year the total fund return was (9.8%), with a three year return of (3.7%) and a five year return of 1.7%. The market value of the fund was \$992.5 million at March 31, 2003.

Ms. Griggs discussed value added by managers, and compared the Teachers' portfolio to the public fund universe. Mr. Moseley reviewed the individual manager returns.

**ITEM 5:** Manager Presentations

**Delaware Investment Advisors** – presenters: Timothy Connors, George Deming and Perry Keck. Delaware currently has \$135 million under management in a domestic equity portfolio, representing 13.6% of the total fund balance. Their return for the quarter ending March 31, 2003, was (5.2%) versus the Russell 1000 Value Index at (4.9%). Delaware's return over the last year was (22.9%) versus the index at (22.8%), and (2.3%) versus the index at (6.9%) over the last three years.

**Putnam Institutional Management** – presenters: Thomas Rosalanko and Christopher Ray. Putnam currently has \$75.9 million under management in an international equity portfolio, representing 7.6% of the total fund balance. Putnam's return for the quarter ending March 31, 2003, was (8.2%) versus the MSCI EAFE Index at (8.2%). Their return since inception on March 31, 2002 was (25.3%) versus the index at (23.2%).

**Lend Lease** – presenters: Joseph Thomas and Scott Brown. Lend Lease Prime Property Fund has a total of \$30.6 million under management in a real estate portfolio, representing 3.1% of the total fund balance. Their return for the quarter ending March 31, 2003, was 2.2% versus 1.3% for the NCREIF Property Index, 8.4% versus the index at 4.9% over the last year, and 7.0% versus the index at 7.8% over the last three years.

Considerable discussion ensued over the pending acquisition of Lend Lease by Morgan Stanley, and the impact to the current team at Lend Lease.

**ITEM 6:** Linda Tuscano Request

**On motion of Mr. Spaulding seconded by Mr. Candon, it was unanimously voted to deny Ms. Tuscano's request to waive the ninety-day timeframe required by statute in which to apply for a disability retirement benefit.**

**ITEM 7:** State Treasurer's Report

The State Treasurer's report was deferred.

**ITEM 8:** Small Cap Value Manager Search

Ten managers were identified as potential candidates in the search conducted by NEPC.

Mr. Kaplan asked NEPC to explain their responses to questions on their RFP submittal for Consultant Services. One response stated they did not have a conflict of interest, yet they hold NEPC, Inc. Mr. Charleton explained that they have never processed money or conducted any trading. NEPC, Inc. is an introducing broker, but not an executing broker. The two execution brokers are paid by NEPC, Inc. to execute the trade. Mr. Charleton confirmed that NEPC's negative response to prior or pending litigation was accurate as well, as Ms. Griggs was not an employee of NEPC when the RFP was prepared.

Discussion of the top ten small cap value manager finalists ensued. Upon a request by the board, NEPC provided their top three recommendations as follows: *Artisan Partners, LP*, *Wedge Capital Management, LLP* and *Trusco Capital Management, Inc.* A fourth candidate, *Wellington Management, Co.* was added to round out the list of finalists. After further discussion, it was the consensus of the board to eliminate *Trusco Capital Management Inc.*, and invite the remaining three to participate in a presentation to the board at an upcoming meeting.

Mr. Harris left the meeting.

**ITEM 9:** Any other investment related business to come before the board

The June 5, 2003, meeting will begin with coffee at 8:00 a.m. followed by the business meeting at 8:15 a.m. Agenda items will include the two outstanding opinions from the Attorney General's Office, as well as discussion of board attendance at the NCTR Annual Convention.

The board agreed to have four investment meetings each year, with business meetings in between the investment meetings, if needed, and two joint board meetings per year if warranted.

Mr. Spaulding reported that Jeff Wilson, Deputy State Treasurer, will be moving back to Manchester sometime during the summer. Mr. Spaulding will be recruiting someone to fill Mr. Wilson's position.

Mr. Mackey requested that the report on the *Impact of the Underfunding in the Teachers' Retirement System* be updated after the FY 2003 valuation.

**On a motion by Mr. Kaplan seconded by Mr. Spaulding, the Board unanimously voted to adjourn at 5:42 p.m.**

Respectfully submitted,

Cynthia L. Webster  
Executive Secretary to the Board